

Lessons from the Global Financial Crisis in the Age of COVID-19

A Virtual Conference co-hosted by the
International Monetary Fund and The University of Tokyo

Session 1: Monday, November 23

International crisis management during the GFC and lessons for the COVID-19 crisis

Intervention of Francesco Papadia

Senior Fellow at Bruegel

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Collaboration was built on a 5 tenets central bank model

- Even if the Friedmanian approach to monetary policy has been superseded by the Wicksellian approach, a tight control of the central bank balance sheet is critical.
- Fiscal and monetary policy should be kept separate and fiscal dominance should be avoided.
- The central bank should concentrate its attention on very short money market rates.
- Resource allocation is no business for the central bank.
- Similarly, the central bank should not engage into income distribution.

Advanced
economies central
banks are now not
respecting any of
these tenets

- Balance sheets have grown by a factor of 10, 5 and 6 respectively for the FED, the ECB and the BOJ and central banks have let other agents influence their balance sheet.
- Institutionally monetary policy and fiscal policy are separate but, with central banks in the US and the €-area holding close to 30% of the stock of government bonds and Japan holding about a half of it there is, de facto, no separation.
- Yield curve control is formally pursued by the BoJ, but various forms of QE in the US, €-area, and the UK de facto pursue a similar goal.
- Targeted refinancing operations in the €-area explicitly favour bank lending to enterprises rather than households; 13.3 FED operations clearly have resource allocation purposes.
- Income distribution has entered among the considerations of central banks, albeit in a soft way.

Are central banks
now following the
prescriptions of
Modern
Monetary
Theory?

- My internal inconsistency:
 - I am still attached to the 5 tenets and think MMT is fallacious.
 - But I mostly approve what central banks are doing
- The only way out of the inconsistency:
 - The deviations from the tenets are temporary and central bank can follow them again when the situation will normalize.

Is central bank collaboration now more difficult because of the deviation from the previous model?

- I have no definitive answer, but 5 concerns, and one attenuating factor:
 1. The move from the sole concentration on the short interest rate as a tool to the emphasis on QE makes collaboration more complicated.
 2. The linkages between fiscal and monetary policy inevitably give a national character to monetary policy
 3. Taking into account resource allocation and income distribution issues, with all their national idiosyncrasies, tends to move central banks towards a more national approach.
 4. Looking from outside, I don't see bursts of collaboration in dealing with COVID 19 like the ones that appeared during the Great recession.
- But the renewal of the swaps is a good sign.

Still two conclusions

- Central bank collaboration is as needed as always.
- We should keep a very keen eye on developments in this area, ready to detect, and possibly counter, deviations from the collaborative behaviour.